

**STATE OF CALIFORNIA
DEPARTMENT OF INSURANCE
45 Fremont Street, 21st Floor
San Francisco, California 94105**

REG-2008-00023

June 17, 2008

INITIAL STATEMENT OF REASONS

TITLE INSURANCE REBATES AND COMMISSIONS

INTRODUCTION

California Insurance Commissioner Steve Poizner will hold a public hearing to consider adoption of proposed regulations governing rebates and commissions involving title insurers, underwritten title companies, and controlled escrow companies, amending Title 10, chapter 5, Subchapter 3, Article 14.

The proposed regulations implement, interpret and make specific the provisions of California Insurance Code Sections 730 et seq., 12389, 12389.1, 12389.2, 12404-12411, 12919, and 12921.

California Insurance Code Section 12404 prohibits a title insurer, underwritten title company or controlled escrow company to pay, directly or indirectly, any commission, compensation, or other consideration to any person as an inducement for the placement or referral of title business. Section 12404(d) provides that reasonable expenditures for food, beverages, entertainment, educational programs, and promotional items constituting ordinary business expenses are deemed not to constitute an inducement for the referral of title business, as specified. The statute does not, however, set explicit standards for reasonable expenditures that do not constitute an inducement. The proposed regulations fill that gap.

Also, the statute does not address a process to monitor compliance with the statute. These proposed regulations establish reporting and documentation requirements to monitor compliance by title marketing and sales representatives employed by, or working on behalf of, the title insurers, underwritten title companies and controlled escrow companies. The proposed amendments also provide for the confidential treatment of the requested information.

Further, the proposed amendments make clear that the Insurance Commissioner may utilize all enforcement remedies provided by statute to enforce the provisions of the regulations and that nothing in the regulations alters the liability of the licensees for the acts of their employees and/or independent contractors.

SPECIFIC PURPOSE OF THE REGULATIONS AND NECESSITY

The specific purpose of each regulation and the rationale for the Commissioner's initial determination that each regulation is reasonably necessary to carry out the purpose for which it is proposed is set forth below.

Section 2555.5 Preamble

The purpose of this section is to describe the objectives of the proposed amendments. Insurance Code §12404 prohibits a title insurer, underwritten title company or controlled escrow company to pay, directly or indirectly, any commission, compensation or other consideration to any person as an inducement for the referral of title business. Section 12404(d) provides that reasonable expenditures for food, beverages, entertainment, educational programs, and promotional items constituting ordinary business expenses are deemed not to constitute an inducement for the referral of title business under specified circumstances. The statute does not, however, set explicit standards for reasonable expenditures that do not constitute an inducement. Also, the statute does not address a process to monitor compliance with the statute to discourage inducements for the referral of title business. The proposed regulations fill these gaps. These regulations delineate standards for reasonable expenditures that are deemed not to constitute an inducement for the referral of business, define a key term, set forth reporting and documentation requirements, and identify enforcement remedies applicable to these regulations.

By describing the objectives of these regulations, this section provides necessary information to licensees so that they have a clear overview of the purpose of the proposed amendments, how the required information will be treated, and the entities to which they apply. Adopting these proposals is necessary to clarify the purpose and objectives of the regulations, to encourage accurate reporting by title entities, and to confirm the confidential treatment of the information received. In this way, licensees will be able to easily identify and understand the scope of the regulations and which entities and activities are subject to them.

Section 2555.6 Definition

Insurance Code §12404 recognizes that marketing practices that utilize illegal rebates to induce the referral of title business harm consumers. The objective of these regulations is to discourage such inducements. To accomplish this objective, the proposed amendments, among other things, establish reporting and record documentation requirements of expenditures by title marketing and sales representatives employed by, or working on behalf of, a title insurer, underwritten title company or controlled escrow company to ensure compliance. The purpose of the new Definition section is to define the key term of "title marketing and/or sales representative," as used in the regulations, to distinguish employees of title entities who are responsible for bringing title business to the title entities from those employees who are responsible for administrative functions. The rationale for this amendment is to avoid confusion and make clear the obligations of insurers. Adopting this proposed regulation is reasonably necessary to ensure that licensees have a clear understanding of which functional persons are subject to the reporting and record documentation requirements to ensure compliance.

Section 2555.7 Standards of Reasonable Expenditures

An illegal rebate to obtain the referral of title business harms consumers as well as the competition. In recognizing the potential for harm, the Legislature enacted Insurance Code §12404 which prohibits a title insurer, underwritten title company or controlled escrow company to pay, directly or indirectly, any commission, compensation or other consideration to any person as an inducement for the referral of title business. Section 12404(d) provides that reasonable expenditures for food, beverages, entertainment, educational programs, and promotional items constituting ordinary business expenses are deemed not to constitute an inducement for the referral of title business under specified circumstances. Although Section 12404(d) of the California Insurance Code provides that certain reasonable expenditures are deemed not to constitute an inducement for the placement or referral of title business, it does not specifically set forth what is a reasonable expenditure.

The purpose of this proposed section is to provide the standards to fill this gap. The rationale for this amendment is to interpret and make specific the obligations of licensees under the statute. Adopting this proposed new section is reasonably necessary to ensure that licensees have a clear understanding of the boundaries of a reasonable expenditure that is deemed not to constitute an inducement for the referral of title business to ensure compliance with the anti-illegal rebate provisions of Insurance Code §12404.

Section 2555.8 Reporting and Record Documentation

An objective of the proposed amendments is to discourage a title insurer, underwritten title company or controlled escrow company from paying, directly or indirectly, any commission, compensation, or other consideration to any person as an inducement for the placement or referral of title business. Section 12404(d) of the California Insurance Code provides that certain reasonable expenditures are deemed not to constitute an inducement for the referral of title business. However, it does not provide for a reporting process or documentation requirement to monitor reasonable expenditures made on behalf of, or benefiting a person, as defined in Insurance Code Section 12404(b)(1) to ensure compliance. This proposed section specifies the reporting and documentation requirements of title insurers, underwritten title companies and controlled escrow companies. The purpose of this new section is to establish uniform standards for a reporting process and maintenance of supporting documentation. In addition, the purpose of this section is to require each title entity to identify, within a reasonable time of employment and termination, whether employed by or independently contracted to the title entity, those individuals who market, offer, solicit, negotiate or sell title insurance on the title entity's behalf. This information is necessary to identify, verify, and confirm the manner and extent of any expenditure made on behalf of the title entity. The rationale for this amendment is to make clear the obligations of licensees to comply with reporting requirements and to discourage illegal rebates. Adopting this proposed section is reasonably necessary to inform licensees as to what information must be collected, maintained, and reported, and the timeframes for such reporting to provide a clear understanding to licensees of such requirements to ensure compliance.

Section 2555.9

Penalties

Existing law, Sections 12409, 12410 and 12411 of the California Insurance Code, provide enforcement remedies to address noncompliance with Section 12404 of the Insurance Code. The purpose of this section is to make clear that the Insurance Commissioner is entitled to utilize any of these enforcement remedies for failure to comply with the provisions of these regulations. In addition, this new section makes explicit that nothing in these regulations alters the liability of an insurer, underwritten title company or controlled escrow company for acts of its employees and/or independent contractors working on their behalf. The rationale for this amendment is to provide notice of enforcement remedies to ensure compliance. Adopting this proposal is reasonably necessary to inform licensees of the enforcement tools that the Commissioner may utilize and potential consequences of noncompliance with these regulations.

IDENTIFICATION OF STUDIES

The Commissioner has not relied upon technical, theoretical, or empirical studies or reports in proposing these regulations.

SPECIFIC ACTIONS, PROCEDURES, TECHNOLOGIES OR EQUIPMENT

Adoption of these regulations would not mandate the use of specific technologies or equipment or prescribe specific actions or procedures.

REASONABLE ALTERNATIVES

The Commissioner invites public comments on reasonable alternatives which would be as effective as, and less burdensome to, affected private persons and small businesses.

ECONOMIC IMPACT ON BUSINESS

The Commissioner has initially determined that the proposed regulations will not have a significant adverse economic impact on businesses because insurers are already required to report, document, and substantiate reasonable expenditures claimed as ordinary business expenses for Internal Revenue Code and internal accounting purposes and the proposed amendments merely clarify existing law. The Commissioner invites interested parties to comment on whether the proposed regulations will have a significant adverse economic impact on business.